IN THE

Supreme Court of the United States

OCTOBER TERM, 1961

No. 115

FEDERAL POWER COMMISSION, *Petitioner*,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY, and UNITED FUEL GAS COMPANY, *Respondents*.

No. 50

CITY OF PITTSBURGH, PENNSYLVANIA, *Petitioner*,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY, and UNITED FUEL GAS COMPANY, *Respondents*.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

BRIEF OF TENNESSEE GAS TRANSMISSION COMPANY IN OPPOSITION

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INDEX

CITATIONS

CASES:

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Petitioner,

v.

TENNESSEE GAS TRANSMISSION COMPANY, THE MANUFACTURERS LIGHT AND HEAT COMPANY, THE OHIO FUEL GAS COMPANY, and UNITED FUEL GAS COMPANY,
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No. 605

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v.

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BRIEF OF TENNESSEE GAS TRANSMISSION COMPANY IN OPPOSITION

OPINION BELOW

The opinions of the Court of Appeals for the Fifth Circuit are reported at 293 F. 2d 761, and printed as Appendix A of the petition in No. 591. The orders

of the Federal Power Commission (R. 524-540, 585-591)[1] are reported at 24 F.P.C. 204 and 525.

JURISDICTION

The jurisdictional requisites are adequately set forth in the petitions.

QUESTIONS PRESENTED

(1) Does the Federal Power Commission have authority under Section 4 of the Natural Gas Act to set aside filed individual zone rates, order reductions in rates and refunds prior to a determination of the zone allocation issue which is an inseparable part of determining whether the filed individual zone rates are just and reasonable?

(2) Where the issue of zone allocation has been thoroughly tried and briefed and is awaiting decision, did the Commission abuse its discretion in failing to decide that issue prior to ordering an interim reduction in rates where such action would in fact deprive Tennessee Gas Transmission Company of earning the rate of return prescribed by the Commission's interim order?

STATUTE INVOLVED

The pertinent provisions of the Natural Gas Act, 52 Stat. 821, as amended, 15 U.S.C. 717-717w, are set out in Appendix B to the petition in No. 591.

[1] The record references "R. ___" are to the pages of the Joint Appendix.

STATEMENT OF THE CASE

This proceeding involves a rate order of the Federal Power Commission, issued August 9, 1960, which required Tennessee Gas Transmission Company (Tennessee) to reduce its rates on an interim basis and make refunds, prior to the resolution of interrelated allocation questions necessary to a determination of which of the zone rates filed by Tennessee were unlawful. Tennessee sought to have the Commission decide the interrelated allocation questions so that it could determine from the Commission's order, which particular rates, if any, should be reduced and to whom refunds were due. The Commission denied Tennessee's request, holding that it had authority to order an interim rate reduction even though it might later find that certain rates in particular zones, which Tennessee was required to reduce on an interim basis, were in fact lawful in the first instance and that Tennessee made refunds, pursuant to the interim order, in the wrong amounts to the wrong persons.

The Court of Appeals for the Fifth Circuit affirmed the Commission's substantive determination of rate of return, but held that the Commission erred in ordering an interim reduction in rates prior to a determination of the allocation issues.

Tennessee owns and operates a natural gas pipeline system extending in a northeasterly direction from its sources of supply in Texas and Louisiana through the States of Texas, Louisiana, Arkansas, Mississippi, Alabama, Tennessee, Kentucky, West Virginia, Ohio, Pennsylvania, New Jersey, New York, Massachusetts, New Hampshire, Rhode Island and Connecticut. The rates charged by Tennessee for the transportation and sales for resale of natural gas in interstate commerce

are subject to the jurisdiction of the Commission under the Natural Gas Act (15 U.S.C. 717-717w). The Tennessee system is divided into six rate zones, with rates differing among the zones to give effect to distance from source of gas supply as well as other factors.

On October 5, 1959, Tennessee filed with the Commission, pursuant to Section 4(d) of the Natural Gas Act, schedules of rate changes designed to recover the increased cost of providing natural gas service (R. 502-504). Among the increased costs sought to be recovered was the increased interest cost on debt incurred in financing expansions of pipeline capacity approved by the Commission. Since interest costs on long-term debt constitute an integral part of the over-all return, Tennessee sought an increase in the rate of return on its investment to 7 percent solely to recover the increased cost of debt. No increase in return to the common stockholders was requested.

The rate schedules filed by Tennessee set forth the respective rates proposed by Tennessee for each class of service in each of the six rate zones on the Tennessee system.

By order issued November 4, 1959, the Commission ordered a hearing to determine the "lawfulness" of the rates which had been filed (R. 502-504). Following a five-month period of suspension, the rates became effective April 5, 1960, subject to an undertaking by Tennessee, required by Commission order, to "refund at such times and in such manner as may be required by final order of the Commission, the portion of the increased rates found by the Commission in this proceeding not justified, together with inter-

est thereon at the rate of 7 percent per annum" (R. 505-509).

Hearings commenced on February 2, 1960, and continued intermittently until recessed on May 25, 1960. During the course of the hearings, Commission Staff Counsel moved that the hearing be divided into two phases, the first phase to deal solely with the issue of rate of return, and the remaining issues to be reserved for a later stage of the proceeding. Staff Counsel further proposed that upon completion of the first phase of the proceeding, the Examiner's decision be omitted; that the Commission issue a decision determining the fair rate of return for Tennessee, and that the Commission issue an interim order requiring Tennessee to reduce its rates and make refunds, in the event the Commission should conclude that the fair rate of return is less than claimed by Tennessee (R. 377-378).

When Staff Counsel made his motion, there was pending before the Commission in the instant proceeding, and in another pending proceeding involving Tennessee (Docket No. G-11980), the issue as to the proper method of allocating Tennessee's cost of service among its six rate zones and various classes of services. Almost a year and one-half prior to the interim order in this case, the Commission had ruled that determination of the allocation issue should be expedited and, to that end, severed that issue for separate and prior hearing and determination in Docket G-11980.[2] At the time Staff Counsel made his motion, the allocation issue had been thoroughly tried and briefed, and was ripe for decision. Additionally, the

[2] *Tennessee Gas Transmission Company*, Docket G-11980, order issued April 30, 1959.

Examiner in the instant proceeding, who is also the Examiner in Docket G-11980, had ruled that the determination of the allocation issue in Docket G-11980 would govern the method of allocating Tennessee's cost of service in this case (R. 50-51).

Since determination of the allocation issue is required in order to translate the cost of service into rates for the various zones and services, Tennessee filed a memorandum opposing the Staff's motion for an interim order on the ground, *inter alia*, that such order would be illegal unless the Commission simultaneously determined the allocation issue (R. 591-606). On July 19, 1960, Tennessee filed a motion with the Commission requesting it to determine the allocation issue simultaneously with the issue of rate of return (R. 519-521). By order issued August 5, 1960, the Commission denied Tennessee's motion (R. 521-523).[3]

On August 9, 1960, the Commission issued its interim order here involved, adopting the Staff's proposed procedure. Although the Commission found that the evidence supported Tennessee's claimed increase in cost of debt (R. 529), it disallowed Tennessee's claimed 7 percent rate of return and fixed a 6⅛ percent rate of return by reducing the allowance on Tennessee's common equity some 26 percent below that which it had allowed as reasonable in a 1957 rate decision.[4] The Commission's order required Tennessee

[3] Petitioner in No. 591 (p. 5) alleges that the motion filed by Tennessee was untimely, but fails to mention the fact that it was not denied on that ground.

[4] In *Tennessee Gas Transmission Company*, 18 F.P.C. 428, 430 (1957), adopting and modifying on other grounds an Examiner's decision at 18 F.P.C. 439, 441, the Commission found that a 13.71% return on common equity was reasonable. In the instant case, the

to file reduced rates retroactively to April 5, 1960, and required Tennessee to make refunds of the differences in rates collected since April 5, 1960 (R. 524-540).

The Commission, however, failed to make any determination as to the proper method of cost allocation which should be employed in allocating the reduced over-all cost of service among the six rate zones and various classes of service on the Tennessee system. Nor did the Commission make a determination or findings as to which of the various zone rates filed by Tennessee were unlawful, which rates should lawfully be reduced, or to whom refunds were lawfully due. Instead, the Commission left these crucial questions open for later decision, even though such later decision might result in a determination that Tennessee had reduced rates in various zones, pursuant to the interim order, which were in fact lawful in the first instance and had made refunds in the wrong amounts to the wrong customers.

Since the Commission's order in effect required Tennessee's stockholders to absorb virtually the entire increase in cost of debt, by reducing the return allowance on equity below that commensurate with returns being earned by other pipelines; and since the requirement of an immediate reduction in rates prior to a determination by the Commission as to how such reduction should be allocated among the six rate zones threatened to deprive Tennessee of the opportunity of even earning the return which the Commission fixed,

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Commission reduced the return on common equity to 10.12% (R. 534). This return on equity was 20% below the *lowest* average return on equity earned by the major pipelines in any year since 1951 (R. 475), and was below the lowest amount earned by the pipeline industry as a whole since 1951. *F.P.C. Statistics of Natural Gas Companies* (1959), p. XII.

Tennessee applied for a rehearing of the Commission's order (R. 541-576). On September 27, 1960, the Commission denied Tennessee's application for rehearing (R. 585-591).

On October 3, 1960, Tennessee filed its Petition to Review with the Fifth Circuit Court of Appeals.[5] As stated above, by its decision issued August 2, 1961, the Court upheld the Commission's substantive determination as to rate of return, but it held that the Commission erred in requiring a reduction in rates and refunds to be made prior to a determination of the pending allocation issues, since the failure to decide the allocation issue threatened to deprive Tennessee of the return which the Commission found proper.

Petitioners in Nos. 591 and 605 contend that the Court below erred in setting aside the portion of the Commission's order dealing with the interim order. Since both petitions seek certiorari to review the same judgment, and since the basic issues raised in both cases are the same, this single brief is filed in opposition to each of the petitions.

ARGUMENT

The decision below follows the rationale of leading cases defining the Commission's authority under the rate provisions of Sections 4 and 5 of the Natural Gas Act. These cases hold that rates filed with the Commission "can be set aside *only* upon being found un-

[5] Tennessee simultaneously filed a motion for stay of the Commission's order, which was denied, Judge Wisdom dissenting. *Tennessee Gas Transmission Company* v. *F.P.C.*, 283 F. 2d 729. After the denial of the stay, Tennessee reduced its rates and made refunds to its customers, subject to its right to recoupment in the event the Commission's order was overturned on appeal.

lawful by the Commission."[6] *United Gas Pipe Line Co. v. Mobile Gas Service Corp.*, 350 U.S. 333, 342 (1956); *Colorado Interstate Gas Co. v. F.P.C.*, 142 F. 2d 943, 954 (10th Cir. 1944), affirmed 324 U.S. 581. The Court below simply held that the same standards apply to an interim rate reduction order as apply to a final rate reduction order issued at the conclusion of the proceeding.

(1) In the case at bar the Commission found that the rates filed by Tennessee were "excessive" (R. 537). However, it had no basis for making such a finding, because a valid determination of whether or not any of the individual zone rates filed by Tennessee are "excessive" and, therefore, unlawful depends not only on a correct decision as to the rate of return, but also as to the proper method of allocating the cost of service among the various zones.

As stated above, the 17-state area in which Tennessee transports and sells natural gas is divided into six established rate zones for rate-making purposes. The aforementioned allocation issue pending before the Commission in the prior rate proceeding involving Tennessee (Docket G-11980) will, when resolved, determine for the first time the proper method of allocating Tennessee's cost of service among the various rate zones and services for the purpose of designing rates. As stated previously, the Examiner has ruled that the determination of the allocation issue in Docket G-11980 will govern the allocation of cost of service in the case at bar.[7]

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[6] Emphasis is supplied throughout this brief unless otherwise indicated.

[7] No appeal from this ruling was taken by any of the parties to the instant proceeding.

The diverse methods of allocation which have been submitted by the parties in the G-11980 proceeding yield such drastically different results, that even if there is a substantial reduction in the over-all cost of service claimed by Tennessee, there may be no reduction in rates in certain zones depending on the allocation method selected (R. 594-595, 598). For example, in the G-11980 proceeding the Commission's Staff claims that Tennessee's total cost of service is approximately $185,700,000. Of this amount, Tennessee's customers in West Virginia[*] (Eastern Zone) contended that under their method of allocation approximately $24,000,000 should be collected from customers in the New England Zone, $62,000,000 from the customers in West Virginia and the balance from customers in the other four zones. Tennessee's New England customers, on the other hand, claim that New England should bear only $16,800,000 of the cost of service and that the West Virginia customers are responsible for almost $68,000,000 (R. 593-96, 598). Tennessee, which claims a higher cost of service than the Staff, predicated its rates on an allocation of approximately $21,000,000 to New England and $72,000,000 to West Virginia. Thus, West Virginia's method of allocation would allocate approximately $3,000,000 more costs to New England than the revenues which Tennessee's filed rates yield in the New England Zone. Hence, even if the Staff's cost of service were adopted, under West Virginia's method of allocation there should be no reduction in rates in New England, since Tennessee's filed rates for that zone would not be excessive.

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[*] The West Virginia method of allocation is sometimes referred to in the record as the "Columbia" method (R. 594-5).

The foregoing demonstrates that it is impossible, without determining the allocation issue, for the Commission to find, as required by the Act, that the specific zone rates filed by Tennessee are unlawful. Here the Commission has only determined that there should be an approximate $11,000,000 *over-all* reduction in the aggregate level of the rates due to the reduced rate of return. However, by reason of its failure to decide the allocation issue, the Commission had no basis for determining which of the filed rates in the six zones are unlawful, the extent that the individual filed rates should be reduced, or to whom refunds were lawfully due. Although these determinations are necessary prerequisites to its action, the Commission's order required Tennessee to reduce its rates in each of the zones and make refunds to customers in each zone at the risk of a later determination by the Commission that Tennessee had reduced rates (pursuant to the interim order) which were in fact lawful in the first instance and had made refunds in the wrong amounts to the wrong customers. Under the Commission's interpretation of the Act, it would have no power retroactively to increase Tennessee's rates back to the originally filed level even though it later found certain of those rates to have been lawful.[9] As Judge Wisdom aptly pointed out below, the Commission failed to "put the horse where he belongs—in front of the cart."[10]

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[9] The Commission interprets the Act as precluding it from increasing rates above those on file with the Commission. *Atlantic Seaboard Corporation*, 11 F.P.C. 43, 63-65 (1952). Since the rates filed by Tennessee were set aside by the interim order, the Commission deems those rates as no longer being on file.

[10] Order issued October 28, 1960, denying motion for stay, dissent, p. 3.

(2) Petitioners contend that the decision of the Court below would outlaw the use of the so-called interim order procedure, even though that procedure was judicially approved in *Federal Power Commission* v. *Natural Gas Pipeline Co.*, 315 U.S. 575 (1942); *Panhandle Eastern Pipe Line Co.* v. *Federal Power Commission*, 236 F. 2d 606 (3d Cir. 1956); and *State Corporation Commission of Kansas* v. *Federal Power Commission*, 206 F. 2d 690 (8th Cir. 1953). They argue that unless this Court strikes down the portion of the Fifth Circuit's decision dealing with the interim order procedure, the Commission will lose a valuable tool "designed to carry out the mandate of Section 4 of the Natural Gas Act that the Commission decide increased rate questions as speedily as possible" (Petition No. 591, pp. 8-9).

The interim order procedure is a procedure whereby the Commission decides issues in a rate case on a piecemeal basis rather than issuing a single decision as to all issues involved. Since this procedure requires more than one decision and a series of briefs, it is highly debatable whether it does, in fact, result in deciding rate cases "as speedily as possible."[11] Indeed, there is growing belief that the interim order procedure retards rather than accelerates the ultimate disposition of rate cases. In point are the following observations of Commissioner Kuykendall recently made in voicing his objections to invoking the interim order procedure in *Cities Service Gas Company*, Order issued November 1, 1961 in Docket RP62-1 (dissent):

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[11] For example, the rates here involved were filed on October 5, 1959. The interim order on rate of return was issued on August 9, 1960. The remaining issues are still pending before the Hearing Examiner.

"I concur in the result, but do not agree with all that is said. I have always had some reservations about the worth of the interim order procedure, but was willing to give it a thorough trial. Our experience has convinced me that its faults outweigh its virtues.

"I now am confident that our rate cases can be handled more expeditiously if we concentrate on complete conclusion of them, rather than taking piece meal action. Furthermore, it is obvious that we are compounding the already excessive amount of litigation which ensues from our decisions." [12]

Contrary to the implication in the petitions, the procedure has not been widely used in the past. In fact, prior to the time the rates here involved were filed, the Commission had invoked this procedure only three times, that we know of, in over 20 years of regulation under the Natural Gas Act.[13]

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[12] It is pertinent to note that in the instant Tennessee case, Commissioner Kuykendall supported the interim-order procedure, dissenting only as to the rate of return allowed. (R. 540)

[13] The interim order procedure has not been used in any case involving rate increases filed by independent producers, notwithstanding the fact that such cases constitute the great bulk of the Commission's backlog of pending cases and were the primary cause for the filing of rate increases by the pipeline companies which purchase gas from such producers. In *Phillips Petroleum Co.*, Opinion 338 (issued September 28, 1960) 24 F.P.C. 537 at 545, 546, the Commission stated that:

"* * * Currently, 570 of these producers are involved in 3,278 producer rate increase filings now under suspension and awaiting hearings and decisions. The number of completions of independent producer rate cases per man-year during the first 6 years following the Phillips decision indicate that nearly 13 years would be required for our present staff to dispose of the 2,313 cases pending on July 1, 1960. Within this 13-year period an additional estimated 6,580 cases would have been received."

In the three previous cases, *supra*, where such procedure has been applied, however, the Commission could and did find that the rates filed were unlawful upon the basis of the interim issues decided. As Commission Counsel conceded on oral argument in the Court below,[14] none of those cases, which are the same three cases now relied on by Petitioners, had pending rate design and allocation issues which could be applied retroactively to change the results of the interim order. Hence, unlike the instant case, the basis upon which interim rates were reduced and refunds were made was final and could not be adjusted retroactively.[15]

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[14] This concession was made at the oral argument on October 19, 1960 (Tr. 36) before the Court below on the motion for stay. The oral argument was transcribed with the Court's permission.

[15] In the *Panhandle* case, *supra*, the Commission, just 75 days prior to the interim order, had decided rate design and allocation issues for the Panhandle system. The interim order made it clear that it would not retry these issues and that the interim reduction in rates should be based on the same allocation method just decided (See 236 F. 2d at p. 611). Thus, as the Court pointed out in the Panhandle case the issues decided on an interim basis were "severable" from the remaining issues in that case (236 F. 2d at 608). The *State Corporation Commission* case, *supra*, which involved an interim reduction in rates for Northern Natural Gas Company, is inapposite because there were no jurisdictional rate zones on the Northern system at the time of the interim order. Since Northern had single system-wide rates, no allocation to zones was necessary. While there was an issue pending as to allocation of costs between jurisdictional and non-jurisdictional gas business, the Commission dismissed that issue in its interim order because a method of allocation had just been prescribed in a previous opinion. Thus, for purposes of allocating costs between jurisdictional and non-jurisdictional business, the Commission adopted the allocation method that had just been prescribed. See *Northern Natural Gas Company*, 11 F.P.C. 278 and 11 F.P.C. 1324 (1952). Since the *Natural Gas Pipeline* case, *supra*, was a Section 5(a) investigation, it is clearly inapposite because under Section 5(a) of the Act the Commission's orders have prospective effect only. Thus, if the Commission had adopted a different method of allocation subse-

Whether or not the interim order procedure is a desirable means of expediting rate cases is really beside the point, for the Court below does not hold that the Commission lacks authority to utilize this procedure. It holds, instead, that in the special circumstances of *this case* it was unlawful and an abuse of discretion for the Commission to order an interim reduction in rates prior to a determination of the pending allocation issue. In so doing, the Court relied on the Commission's own decision in an earlier Tennessee rate case involving similar circumstances where the Commission itself refused to adopt the interim order procedure on the ground that it would be "premature," "unfair" and "improper" to issue an interim order before determining the pending allocation issue. The following reasons given by the Commission in its earlier decision for refusing to fix interim rates prior to a determination of the pending allocation issue provide powerful support for the decision of the Court below: [16]

> "The pleadings pose the questions of whether it is appropriate and in the public interest for the Commission *at this time* and *on the present record* to consider and determine separately the issues relating to total cost of service and rate level and to reserve for subsequent decision the issue raised

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quent to the interim order, it could not have been applied retroactively. For this reason, as the Court of Appeals noted in the *Natural Gas Pipeline* case, the interim order procedure could in no way injure the pipeline company in that case (120 F. 2d 625, 631). It is significant to point out that although Judge Tuttle dissented below, he did not claim that the majority decision was in conflict with the above cases.

[16] *Tennessee Gas Transmission Company*, Docket G-5259, Order issued September 20, 1956, mimeo. pp. 3, 5, 6. Tennessee took the position in that case that the cost of service issues could be separated from the allocation issues if the Commission, upon deciding the allocation issue would apply it *prospectively only*.

concerning zone rate differentials; and should the intermediate decision procedure be omitted.

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"* * * Since Tennessee is engaged in rendering jurisdictional and non-jurisdictional service, it is not possible to translate the 'total' of Tennessee's cost of service into jurisdictional 'rate level' without first determining the portion of the 'total' properly allocable to jurisdictional sales. Accordingly, even though we find that it is now appropriate to determine the 'total' of Tennessee's cost of service, such cost of service cannot be translated into jurisdictional rates (or 'rate level') until decision is made as to the proper method of allocating the 'total' between jurisdictional and non-jurisdictional sales.

"Fulfillment of the request of Tennessee that determination be now made as to its total cost of service and the rate level would not only require determination as to the proper method of allocating the 'total' between jurisdictional and non-jurisdictional sales, but it would require also present determination as to the proper method of allocating the jurisdictional portion of the 'total' between the several zones of service, or, at least, a determination that the present zone boundaries and rate differentials should be maintained for sales made on and since December 15, 1954, and continuing until final order in this proceeding. It is not possible at this incomplete state of the proceeding to determine proper zone boundaries and what method of allocating costs between zones would be fair and equitable.

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"* * * our experience tells us that, if *in the future* a change in Tennessee's zone boundaries or rate differentials is in order, the effect of the resultant rate on particular customers will differ dependent upon what cost of service is found

proper here. On this record, however, it is not possible to now determine what the effect upon particular customers will be until resolution of the cost of service and zone issues.

"Thus, we are of the opinion that it would be not only premature for us to grant that part of Tennessee's motion requesting that we at this time fix rates to be effective on and after December 15, 1954, it would also be *unfair and improper.*"

As the Commission recognized above, it cannot separate what is inextricably joined together. In order to determine which of Tennessee's zone rates are excessive and, therefore, unlawful as a result of the interim issue decided, the Commission, admittedly, must determine the allocation issue. In setting aside rates which it may later find lawful, the Commission clearly exceeded its authority under the Act, for, as pointed out above, this Court has held that, rates filed with the Commission "can be set aside *only* upon being found unlawful by the Commission." *United Gas Pipe Line Co.* v. *Mobile Gas Service Corp.*, 350 U.S. 333, 342 (1956).

(3) While the Commission concedes that its failure to determine the allocation issue may result in Tennessee not being able to earn the return which the Commission found proper, it claims that Tennessee cannot be heard to complain because Tennessee has the burden of justifying its rates on the basis of its own presentation (Petition, pp. 15-16). To be sure, Tennessee does have the burden of proof. But we fail to understand—nor did the Court below—how the Commission can validly argue that Tennessee cannot be heard to complain about an order which determines that consumers are entitled to an approximate $11,000,000 reduction in

rates as a result of the rate of return determination, but they establishes a procedure which may require Tennessee to reduce its rates by *more* than $11,000,000.

The undertaking filed by Tennessee and prescribed by the Commission, when the originally filed rates here involved became effective, was that Tennessee would "refund at such times and in such manner as may be required by final order of the Commission, *the portion of the increased rates found by the Commission in this proceeding not justified,* together with interest thereon at the rate of 7 percent per annum" (R. 507-509). Neither the Act nor Tennessee's refund obligation entitled the consumer to reduced rates or refunds in excess of the portion of Tennessee's rates found not lawfully justified, and the Commission has no authority to require Tennessee to reduce its rates or make refunds until it properly determines which of Tennessee's respective zone rates is in fact not lawfully justified.

(4) The Commission contends, however, that the possibility of Tennessee being harmed by the interim order is remote because (1) the presiding examiner has concluded in his recommended decision that Tennessee's allocation method should be adopted by the Commission without substantial modification; and (2) the Commission's staff is advocating in the second phase of the reserved hearing a total cost of service about $36,000,000 less than that contended for by Tennessee [17] (Petition, p. 15, fn. 14). Such contentions are obviously lacking in substance because they are based upon speculation as to the future outcome of these

[17] There is nothing in the record which supports Pittsburgh's assertion that past experience (based on rate cases concluded in fiscal 1961) indicates that "a substantial portion of the total increases will be found unjustified" (Pittsburgh's petition, p. 11).

undecided issues. Any conclusion at this time that Tennessee will not be harmed by the interim order necessarily involves a prejudgment of the Commission's final decision of these undecided matters.

At best, such contentions amount to nothing more than an observation that this proceeding may become moot if the Commission should agree with the Examiner's recommended decision on the allocation issue, assuming, of course, that no appeal is taken from the Commission's decision by parties other than Tennessee.

(5) The petitions of the Commission (pp. 10-12, 17-20) and the City of Pittsburgh (pp. 9-12) attempt to justify the interim order on the grounds of expediency. They argue that unless the Commission can set aside rates on an interim basis prior to a determination of their lawfulness, it will delay refunds to consumers. But such contention begs the fundamental question of whether the interim order is lawful under the special facts and circumstances of this case. No one questions the desirability of expediting hearings and decisions of rate proceedings before the Commission. Here, however, the Commission, in its haste to get partial refunds into the hands of Tennessee's customers, failed to decide the all-important allocation issue, and thereby failed to make the required findings as to which particular rates in the individual zones were unlawful. It, therefore, failed to determine what refunds were *lawfully* due to which customers in the various zones, thereby jeopardizing Tennessee's ability to recover the very return which the Commisson found proper. For Tennessee cannot recoup (through retroactive rate increases) refunds required by the interim order to be made to customers which the Commission may later

find, when it finally decides the allocation issue, were not entitled to such refunds.

The Commission's interim order procedure thus presents a case of "haste making waste"—a situation which could have been readily avoided by simply deciding the allocation issue (then ripe for decision) simultaneously with the rate of return issue.[18]

Additionally, the assertion by the Commission (Petition, p. 11) that pipelines gain by the delay in disposition of refund money because they provide a cheap source of expansion capital is completely without substance and is a gross misconception of financial fact. Apart from the fact that there is no support for the assertion that pipelines deliberately file "excessive" rates, the Commission erroneously states that the 7 percent interest which it requires pipelines to pay on refunds is not an effective deterrent to "excessive" rate filings, because the interest is tax deductible. Thus, the Commission argues, the effective cost to the pipeline is approximately one-half the 7 percent interest rate. The fact is, however, that the cost to the pipeline before taxes is more than 14 percent and after the tax deduction it is 7 percent.

Money collected subject to refund is used (1) to pay operating expenses, (2) to provide additional income to which the pipeline company feels it is en-

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[18] The implication in the petitions that great harm would have been caused to consumers by delaying a reduction in rates until disposition of the allocation issue is without merit. The approximate $11,000,000 reduction in rates ordered by the Commission would result in a savings of less than 15¢ per month to the typical householder. See, Reply of Tennessee Gas Transmission Company to Opposition of the Federal Power Commission to Motion for Stay, pp. 2-3, submitted below in Case No. 18547 on October 14, 1960.

titled, or (3) both. To the extent such money, or any part of it, is required to pay operating expenses, it is obviously not available for expansion purposes.

To the extent it provides additional income, such amount is taxable at the full corporate rate and 52 cents of each dollar is promptly paid to the government as federal income taxes, leaving only 48 cents of each dollar available to the company for expansion or other company purposes.

This result is ignored by the Commission in asserting (Petition, p. 11) that the pipelines' obligation to pay interest on refunds cannot be regarded as an effective deterrent to "excessive" rate filings. The required payment of 7 percent interest on each dollar received in order to have 48 cents available for expansion results in an effective interest cost of 14.5833 percent. Concurrently, Tennessee had bank notes outstanding on which it paid 4.375 per cent interest (R. 486). The entire principal amount borrowed on such bank notes is available for expansion or other company purposes.

The comparison of this 4.375 percent interest rate with the 14.5833 percent rate, resulting from 7 percent interest on refunds, demonstrates the harsh effectiveness of the deterrent. It is true that interest paid is deductible for income tax purposes; however, application of the 52 percent tax rate merely reduces the 14.5833 percent interest rate to 7 percent net effect after taxes. By the same token, the 4.375 percent interest on bank notes is reduced to 2.2728 percent net after taxes. Thus, the tax deduction does not alter the comparison nor the effectiveness of the deterrent. Hence, the contention that pipelines file "excessive"

rates to obtain a cheap source of expansion capital is without any foundation in fact or reason.[19]

(6) Although the Commission concedes that the Court's decision "emphasizes" the special circumstances present in this case, it argues that the decision "appears to have wide application" (Petition, p. 17). But the Commission has experienced no difficulty in applying the interim order procedure since the issuance of the Court's decision in this case. Recently, the Commission granted a motion by its Staff to invoke the interim order procedure in a rate proceeding involving El Paso Natural Gas Company, wherein the Staff urged that:[20]

> "* * * the *Tennessee* decision (*Tennessee Gas Transmission Company* v. *F.P.C.*, 293 F. 2d 761) is distinguishable from these proceedings in that here there are no other issues ripe for decision whereas in *Tennessee* the basis of the court's refusal to allow the interim order to become effective was the fact that the allocation issue was ripe for decision; * * *."

As we read the Court's decision, it would only prevent the Commission from ordering an interim reduction in rates when it has not determined those issues necessary to a finding that the rates filed are in fact unlawful. Contrary to the Commission's assertions, allocation of costs among zones is not an issue in "virtually every major pipeline case." Only a few of the rate cases decided by the Commission in more than

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[19] There is no reason why pipelines should be deterred from filing needed increases in rates. The proper purpose of the interest charge on refunds is to compensate the consumers, not to penalize pipelines for having filed a rate increase.

[20] *El Paso Natural Gas Co.*, Docket No. G-4769, *et al*, order issued December 27, 1961. For the convenience of the Court, a copy of said order is attached hereto as Appendix A.

twenty years have involved this issue and once the Commission decides the issue, it has held that it will not retry it in another case unless there has been a substantial change in circumstances.[21]

Indeed, since the Commission has issued no rules nor prescribed any general method with regard to zone allocation, and since the few previous Commission decisions involving this issue have applied widely different methods, it is virtually impossible for a pipeline to predict what zone allocation method the Commission will adopt for rate-making purposes. By requiring Tennessee to guess, at its peril, what allocation method the Commission will later adopt, the Commission would relegate rate filings into a "poker game" in which only the pipeline could be the loser.[22] The Court below holds that it was unfair and improper for the Commission to adopt such a procedure in a case such as this, when it could result in Tennessee being deprived of revenues needed to meet the cost of providing a valuable service upon which the public depends. It was particularly unfair here because the Commission could have readily resolved the problem by deciding the allocation issue which was ripe for decision.[23]

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[21] For example, as pointed out above, in this very case the Examiner has ruled that the decision as to allocation in Docket G-11980 will apply to the instant case. Also see, *Panhandle Eastern Pipe Line Company* v. *F.P.C.*, *supra*, where the Commission refused to retry the allocation issue because there had been no substantial change in circumstances.

[22] As this Court has aptly observed, allocation of costs "is not a matter for the slide rule," but instead "involves judgment on a myriad of facts." *Colorado Interstate Gas Co.* v. *F.P.C.*, 324 U.S. 581, 589 (1945).

[23] The Commission argues (Petition, p. 16) that since the allocation issue was complex, the Commission properly denied Tennessee's request to omit the intermediate decision on allocation so

In summary, the petitions should be denied not only because the decision below is correct, but also because it does not conflict with any previous decisions, and is admittedly based on the peculiar facts and circumstances connected with this case, and, therefore, is not likely to have broad applicability.

CONCLUSION

In view of the foregoing, we respectfully urge that the Petitions for Certiorari be denied.

Respectfully submitted,

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January 9, 1962

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that it could be decided simultaneously with the rate of return issue. But the Court below does not hold that the Commission erred by not omitttting the intermediate decision on allocation. It holds that the Commission erred in ordering a reduction in rates prior to a decision on allocation. Moreover, it should be noted that the record on rate of return was also complex, but the Commission omitted the intermediate decision on that issue (R. 513-516).

APPENDIX A

UNITED STATES OF AMERICA
FEDERAL POWER COMMISSION

Before Commissioners: Joseph C. Swidler, Chairman; Jerome K. Kuykendall, Howard Morgan, L. J. O'Connor, Jr., and Charles R. Ross.

Docket Nos. G-4769, G-12948, G-17929 and RP60-3
EL PASO NATURAL GAS COMPANY

Order Adopting Interim Order Procedure Omitting Intermediate Decision and Fixing Dates for Filing of Briefs

(Issued December 27, 1961)

The Presiding Examiner, on November 30, 1961, certified to the Commission the record made in these dockets since July 24, 1961 relevant and material to the issue of rate of return, and a motion entered orally upon the record by staff counsel during the hearing on November 16, 1961. In that motion staff counsel requested (1) application in these proceedings of the interim order procedure with respect to the issue of rate of return, and (2) waiver of the intermediate decision procedure in accordance with Section 1.30 of the Commission's Rules of Practice and Procedure and immediate certification of the issue of rate of return, with the testimony and exhibits related thereto, to the Commission for decision on that issue. Several intervenors supported the motion while El Paso objected to it both on the record and by written answer filed November 27, 1961.

It is contemplated that El Paso will be required to reduce its present rates if it is determined under the interim order procedure that the fair rate of return for El Paso is less than that requested in RP60-3. If the fair rate of return is less than that requested in Docket Nos. G-4769, G-12948 and G-17929, it is contemplated that immediate refunds would be ordered in only Docket No. G-4769, for reasons hereinafter stated. Refunds, if necessary, in Docket Nos.

G-12948, G-17929 and RP60-3 would not be ordered until determination of all the issues in those proceedings. It is further contemplated that for purposes of refund and reduced rates, all other factors relating to rate base, cost of service, allocation, etc., will be used as presented by El Paso on the record, without prejudice to the rights of any party to question any of those items in subsequent phases of this proceeding, if such item is determined to be in issue by the Presiding Examiner.

Staff counsel asserts that the interim order procedure is necessary and proper in these proceedings, will expedite these proceedings and will result in substantial justice to El Paso and its customers. In support of his motion staff counsel contends: (1) As the only issue in Docket No. G-4769 is that of a fair return on El Paso's production properties, pursuant to the remand by the Fifth Circuit Court of Appeals, 281 F. 2d 567, the granting of the motion would dispose of that case finally; (2) the Commission, in considering the rate of return issue for the purpose of finally deciding G-4769, will necessarily be reviewing the identical record which relates to the rate of return issue in the latter three dockets; (3) a prompt decision on rate of return could give immediate relief to all of El Paso's customers, particularly those in California which take the bulk of El Paso's gas; (4) the *Tennessee* decision (*Tennessee Gas Transmission Company* v. *F.P.C.*, 293 F. 2d 761) is distinguishable from these proceedings in that here there are no other issues ripe for decision whereas in *Tennessee* the basis of the court's refusal to allow the interim order to become effective was the fact that the allocation issue was ripe for decision; and (5) if the Commission should find that a lesser rate of return is just and reasonable, than that requested by El Paso in Docket Nos. G-12948, G-17929 and RP60-3, it is suggested that a deferral of refunds until final decision of all issues in those proceedings would enable El Paso to earn the rate of return finally determined by the Commission even if the Commission in

its final decision, should change El Paso's allocation method.

El Paso, in its answer to staff counsel's motion, in addition to prematurely arguing the merits of its evidence on rate of return, also contends and argues that: (1) to grant such a motion under the circumstances of this case would be unlawful; (2) even if it were not unlawful, to grant a motion for interim order in this case would be unfair, unwise and not in the public interest; (3) the Presiding Examiner does not have power to grant a motion for interim order procedure in these cases and (4) the motion for omission of the intermediate decision should be denied, because to grant such a motion in this case would be unlawful and even if it could lawfully be done, intermediate decision should not be omitted here.

The Presiding Examiner, in his ruling of November 30, 1961, on staff counsel's motion, granted staff's request for certification of the record on the issue of rate of return. The Examiner found that the waiver of the intermediate decision procedure, and the use of the interim order procedure (pursuant to the Commission's order of November 1, 1961, in *Cities Service Gas Company*, Docket No. RP62-1) will expedite these proceedings and, "with the reservations and conditions proposed by the staff, modified, if the Commission should find that necessary or desirable, be just to all of the parties to these proceedings." The Presiding Examiner then certified the record relating to the rate of return issue to the Commission, as requested in the staff's motion.

El Paso, on December 5, 1961, filed its "Appeal by El Paso Natural Gas Company from Presiding Examiner's Ruling On Motion to Certify; Motion Requesting Opportunity to File Briefs; and Motion Requesting Opportunity to Present Oral Argument." El Paso repeats therein the arguments contained in its answer to staff's motion. El Paso also contends that the Presiding Examiner's find-

ings in his ruling on staff counsel's motion were not made through the exercise of any discretion conferred upon him by the Rules but because the Examiner considers himself bound by the Commission's order of November 1, 1961 in Docket No. RP62-1, "as committing to him for initial decision only the question 'whether the use of the procedure [interim order] will expedite this proceeding and be just to the parties . . .' ". El Paso alleges that the Examiner's finding decides only part of the issues relating to the interim order procedure and that such a method, as set out by the Commission in its *Cities Service* order would, "to no good purpose, fragment the decision-making process and prevent any benefit from being derived from initial decision by the Examiner." For these reasons, El Paso requests the Commission to remand these proceedings to the Examiner for his decision on the question of the propriety of the use of the interim order procedure in these proceedings, taking into account "*all*" of the factors which bear on that problem. However, El Paso fails to point to any factors (other than those covered by the Presiding Examiner in his certification) which it believes relate to the propriety of the use of the interim order procedure. Further, we cannot agree with El Paso's contention that the Presiding Examiner's finding that the procedures proposed by the staff "would expedite the disposition of the proceedings" and "would be just to all of the parties to the proceeding" was based on less than "all" the factors bearing on the problem.

The Commission finds:

(1) The use of the interim order procedure with respect to the rate of return issue in these proceedings is both necessary and proper and will expedite these proceedings and result in substantial justice to all parties.

(2) The staff's motion for application of the interim order procedure and waiver of the intermediate decision with respect to the rate of return issue should be granted

and the parties should be allowed to file briefs as hereinafter provided.

(3) El Paso's "Appeal From Presiding Examiner's Ruling on Motion To Certify; Motion Requesting Opportunity To File Briefs; And Motion Requesting Opportunity To Present Oral Argument" should be denied.

The Commission orders:

(A) The issue of a proper rate of return for El Paso in these proceedings shall be determined under interim order procedure.

(B) The intermediate decision procedure hereby is omitted for purposes of determination of the proper rate of return for El Paso.

(C) El Paso's "Appeal From Presiding Examiner's Ruling On Motion To Certify; Motion Requesting Opportunity To File Briefs; And Motion Requesting Opportunity To Present Oral Argument" hereby is denied.

(D) Main briefs on the issue specified in Paragraph (A) above shall be filed by all parties who desire to do so on or before January 22, 1962, and reply briefs, if any, shall be filed on or before February 2, 1962.

By the Commission. Commissioner Kuykendall dissenting.

J. H. Gutride,
Joseph H. Gutride,
Secretary.